

Agricultural Cooperatives

A Guide to Complying with the Missouri Securities Laws



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Organizing an Agricultural Cooperative

Farmers seeking to organize cooperatives generally are seeking the benefits of economies of scale. Many farmers with common interests may organize through cooperatives and strengthen their market power. Many Missourians in the agriculture industry are also adding value to their products through the efforts of cooperatives. Missouri securities laws recognize this need, while also balancing the need to provide some minimum protection to participants in these cooperatives.

The Missouri Securities Division regulates the offer and sale of securities in the state of Missouri. Shares of stock, membership interests and ownership rights in an agricultural cooperative ("cooperative") are generally considered securities under the Missouri Securities Act of 2003 (the "2003 Act"). Debt or notes issued by a cooperative are also considered securities under the 2003 Act. Under Missouri law, all securities offered or sold in Missouri must be either registered with the commissioner of securities, be exempt from registration or be a federal covered security.

Nonprofit Membership Cooperatives – Securities Exempt from Registration under §409.2-202(8) of the 2003 Act

A member's or owner's interest in a cooperative organized under the Nonprofit Cooperative Marketing Law (Chapter 274, RSMo) may be exempt from securities registration pursuant to §409.2-202(8), RSMo. These securities are exempt if the cooperative is organized and operated as a nonprofit membership cooperative. In addition, the member's or owner's interest can only be sold to bona fide members of the cooperative. No notice filing needs to be made with the Securities Division under the exemption of §409.2-202(8).

New Generation Processing Entity – Securities Exempt from Registration under Missouri rule 15 CSR 30- 54.190

New generation processing entities may also be exempt from securities registration under a rule adopted by the commissioner of securities. A "new generation processing entity" is defined in rule 15 CSR 30-54.190 as:

A partnership, corporation, cooperative, or limited liability organized or incorporated pursuant to the laws of

Missouri consisting of not less than twelve members, approved by the Missouri Agricultural and Small Business Authority, for the purpose of owning or operating within Missouri a development facility or a renewable fuel production facility in which producer members:

- (a) Hold a majority of the governance voting rights of the entity and any governing committee;
- (b) Control the hiring of management; and
- (c) Deliver agricultural commodities or products to the entity for processing, unless multiple processing is required by multiple entities.

The securities issued by a new generation processing entity are exempt from registration if a notice filing is made with the Securities Division in compliance with rule 15 CSR 30-54.190. The notice filing would generally consist of the following: (1) a completed form SE-1, Statement of Claim for the Exemption of Securities for New Generation Processing Entity; (2) Form U-2, Consent to Service of Process; (3) Form U-2A, Uniform Form of Corporate Resolution; and (4) a copy of the prospectus or offering document and other related documents. The regulation further explains the minimum disclosure required in the offering document. In addition, all proceeds must be held in escrow until the Missouri Agricultural

and Small Business Development Authority provides final approval for the new generation processing entity to receive the new generation cooperative incentive tax credits. Note that the notice filing under this exemption may require the assistance of professionals with experience in securities law.

Cooperatives Exempt from Tax under 521 of the Internal Revenue Code – Federal Covered Securities under the 2003 Act

The securities of a cooperative, in which the cooperative receives notice from the Internal Revenue Service that the cooperative is exempt from tax under section 521 of the Internal Revenue Code of 1954, are federal covered securities and registration under Missouri law is not required. Under the 2003 Act, the cooperative issuing these federal covered securities is not required to make any filing with the Securities Division. However, a cooperative selling these federal covered securities in Missouri is still subject to the anti-fraud provisions of the 2003 Act, and therefore, must disclose all material facts concerning the offering to purchasers.

Registration of Securities under the 2003 Act

A cooperative may seek to register its securities with the commissioner of securities pursuant to §409.3-303 or §409.3-304 under the 2003 Act. If the cooperative will be offering and selling its securities to Missouri residents only, then the cooperative may pursue a registration by qualification under §409.3-304. A cooperative registering its securities under §409.3-304 may utilize the form SR-1. The registration statement filed with the Securities Division is generally very comprehensive. The cooperative would probably need to consult with professionals experienced in securities law to complete the registration statement.

Individuals Offering and Selling Securities of a Cooperative May Be Exempt from Registration as an Agent under §409.4-402(a)(3) of the 2003 Act

Under §409.4-402(a)(3), an individual is exempt from registration as an agent if the individual represents an issuer with respect to an offer or sale of the issuer's own securities and is not compensated in connection with the individual's participation by the payment of commission or other remuneration on transactions in

those securities. Under this exemption of agent for the individual, no filing needs to be made with the Securities Division. If an individual would receive a commission or other remuneration on transactions in those securities, then the individual must register under §409.4-406. An individual required to register as an agent under the 2003 Act should contact the Licensing Unit of the Securities Division for further information about registration.

Seed Capital for Developing an Agricultural Cooperative

Individual farmers or a cooperative that is in the early development stage may want to rely on a private offering exemption under the 2003 Act to raise seed capital. This seed capital may be needed to pay for initial start-up costs such as accounting and legal fees and a feasibility study. An exemption that farmers might consider in raising seed capital for a cooperative is contained in §409.2-202(14). The farmers would need to organize sufficiently as an association or cooperative to create an “issuer” under this exemption.

Limited Offering Exemption - §409.2-202(14) of the 2003 Act

Section 409.2-202(14) provides for an exemption from registration for the sale of securities by an issuer to not more than 25 purchasers in Missouri. Under this exemption there can be no general solicitation or general advertising made in connection with the offer to sell or sale of the securities. No commission or other remuneration can be paid to a person for soliciting a purchaser in Missouri under this exemption. In addition, the issuer needs to reasonably believe that the investors are purchasing for investment purposes and not for immediate resale.

No notice filing to the Commissioner is required under this exemption. Note that anyone who sells a security must still make full disclosure of all material facts to any potential investors. Farmers using this exemption to raise seed capital should be mindful about providing important information to other farmers investing seed capital. The seed capital investment itself should be in writing and accurately reflect the amount of the investment and the rights of both the investor and the issuer.

No general solicitation or general advertising is allowed in offering or selling securities under this exemp-

tion. If you solicit, advertise, promote or even seek through direct personal contact to develop leads with anyone but prior acquaintances, you risk losing your exemption from registration and violating the law. This exemption is intended to allow an issuer to raise capital from a network of people with whom you have a preexisting relationship. This acquaintance may be personal or business in nature. This relationship generally would be one of sufficient familiarity to enable a reasonably prudent person to already be aware of the character and general business and financial circumstances of the individuals raising capital.

Proving an Exemption

The burden of proving any exemption is on the person claiming that he or she complied with the requirements of the exemption. Some exemptions are used frequently, but organizers should study the exemptions carefully. It is not a defense that an issuer thought an exemption was applicable. Anyone who sells a security without registration or valid exemption creates liability to all purchasers of the securities for the amount of the purchase plus 8% interest. In addition, the seller may be subject to criminal prosecution of a felony, punishable by 10 years in prison, a \$1,000,000 fine or both.

Violators may also be subject to orders of restitution, disgorgement, rescission and civil penalties. For this reason, it is extremely important to comply with all requirements of the securities laws. In addition, keep in mind that the explanations in this pamphlet are general and anyone making a securities offering should review the actual statutes and regulations prior to effecting a securities transaction.

Material Facts

An exemption from registration is not an exemption from the antifraud provisions of the 2003 Act. A seller of securities is responsible for disclosing all material facts concerning a proposed transaction to the prospective investor. A material fact is any fact that may have an impact on that individual's decision to invest. For that reason, the less involved the prospective investor is with the current operations of the issuer seeking to raise capital, the greater the need to give additional disclosure. A written disclosure document that sets out all the material facts may be a very worthwhile protection. Any person who violates the antifraud provisions in §409.5-501 is subject to civil liability and to criminal prosecution.

Assistance from the Secretary of State

The Missouri Securities Division is a division of the Office of the Secretary of State. The staff of the Securities Division is available to answer questions you may have concerning capital formation and the securities laws between the hours of 8 a.m. to 5 p.m., Monday through Friday.

For more information, contact:

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